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No. 137

IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

MASSACHUSETTS TRUSTEES OF EASTERN GAS AND FUEL ASSOCIATES, *Petitioners*,

v.

UNITED STATES OF AMERICA

On Writ of Certiorari to the United States Court of Appeals for the First Circuit

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BRIEF FOR PETITIONERS

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BRIEF FOR PETITIONERS

OPINIONS BELOW

The opinions of the district court (R. 5-25) are reported at 202 F. Supp. 297 and 210 F. Supp. 822. The opinion of the court of appeals (R. 247-260) is reported at 312 F. 2d 214.[1]

[1] The record herein consists of the appendices printed for the use of the court below, to which have been added the opinion and judgment of that court. This brief is accompanied by a separate document containing Appendices A and B. Appendix A ("A. ....") contains the recent unreported decision of *American President Lines, Ltd.* v. *United States* (N.D. Cal., Oct. 10, 1963). Appendix B ("B. ....") contains portions of the legislative history which are too lengthy to be conveniently set forth as footnotes to the brief.

JURISDICTION

The judgment of the court of appeals was entered January 8, 1963 (R. 260). On March 26, 1963, the time to file a petition for certiorari was extended to and including June 7, 1963 (R. 261). The petition was filed on May 16, 1963, and was granted on October 14, 1963 (R. 262), ... U.S. ... Jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

1. Petitioners bareboat chartered vessels in 1946 from the former United States Maritime Commission ("Maritime") under section 5 of the Merchant Ship Sales Act of 1946. That section provided for an annual charter hire of not less than 15 percent of the sales price of the vessels chartered and for the inclusion in all charters of the terms of section 709(a) of the Merchant Marine Act, 1936, which specified a 50 percent division with the Government of profits earned by the chartered vessels. Maritime promulgated a form of charter which substituted a sliding scale of profit sharing up to 90 percent for the statutory 50 percent.

> The first question is whether Maritime was authorized to increase the 50 percent share of profits specified by section 709(a) to the sliding scale shares up to 90 percent.

2. In mid-1947, a sharp decline occurred in shipping, and Maritime, foreseeing a reduction of its share of profits because of losses anticipated later in that year, gave petitioners fifteen days' notice of termination of the charter as of September 1, 1947, but permitted the charter to continue upon condition that losses

from voyages after September 1 not be offset or averaged with the profits from voyages prior to that date in computing the profits to be paid to Maritime.

The second question is whether this requirement, dividing the calendar year 1947 into two parts for profit sharing computations, violated the provisions of section 709(a) prescribing "calendar year" accounting of "cumulative" net profits.

STATEMENT OF THE CASE AND THE STATUTES INVOLVED

1. The Merchant Ship Sales Act of 1946 (60 Stat. 41; 50 U.S.C. App. §§ 1735-1746, approved March 8, 1946) was designed to rehabilitate the private merchant marine, whose operations had been disrupted and fleets decimated by World War II losses and requisition. Section 7(b)[2] of the act provided that the Maritime Commission ("Maritime") should withdraw all surplus war-built vessels from governmental operation and sell or charter them to American companies for private commercial operation. Section 7(a) of the act provided that Maritime should "so far as practicable and consistent with the policies of this Act"

[2] Section 7(b) of the 1946 Act (50 U.S.C. App. § 1740) provided:

After the cessation of hostilities, operation of vessels in commercial service by the United States, either for its own account or through operating agents under agency agreements, shall, except as to the Panama Railroad Company and other services specifically authorized by law, be continued only to the extent necessary to effect orderly transfer of vessels to private operation.

give preference to citizen applicants to purchase over citizen applicants to charter.[3]

2. Maritime's authority with respect to fixing of the monetary terms of charter hire was contained in section 5 of the 1946 Act (50 U.S.C. App. § 1738). Subsection (b) of section 5 provided:

> The charter hire for any vessel chartered under the provisions of this section shall be fixed by the Commission at such rate as the Commission determines to be consistent with the policies of this Act, but, except upon the affirmative vote of not less than four members of the Commission, such rate shall not be less than 15 per centum per annum of the statutory sales price (computed as of the date of charter). . . . [R]ates of charter hire fixed by the Commission on any war-built vessel which differ from the rate specified in this subsection shall not be less than the prevailing world market charter rate for similar vessels for similar use as determined by the Commission.

Subsection (c) of section 5 provided:

> The provisions of section 708, *709*, 710, 712, and 713, of the Merchant Marine Act, 1936, as

[3] Section 7(a) of the 1946 Act (50 U.S.C. App. § 1740) provided:

> In exercising its powers under this Act and under other provisions of law with respect to the sale and charter of war-built vessels, the Commission shall . . . as between citizen applicants to purchase and citizen applicants to charter . . . so far as practicable and consistent with the policies of this Act, give preference to citizen applicants to purchase. In determining the order of preference between citizen applicants to purchase or between citizen applicants to charter, the Commission shall consider, among other relevant factors, the extent to which losses and requisitions of the applicant's prewar tonnage have been overcome and shall in all cases, in the sale and charter of a war-built vessel, give preference in such sale or charter, as the case may be, to the former owner of such vessel, or to the person for whom the vessel was constructed but to whom delivery thereof was prevented by the United States. . . .

amended, *shall be applicable to charters made under this section.*[4]

And section 709(a) of the 1936 Act (49 Stat. 2010; 46 U.S.C. § 1199) thus made a part of section 5 provided:

> *Every charter made by the Commission pursuant to the provisions of this title shall provide* that whenever, at the end of any calendar year subsequent to the execution of such charter, the cumulative net voyage profits (after payment of the charter hire reserved in the charter and payment of the charterer's fair and reasonable overhead expenses applicable to operation of the charterer vessels) shall exceed 10 per centum per annum on the charaterer's capital necessarily employed in the business of such chartered vessels, the charterer shall pay over to the Commission, as additional charter hire, *one-half* of such cumulative net voyage profit in excess of 10 per centum per annum; *Provided,* That the cumulative net profit so accounted for shall not be included in any calculation of cumulative net profit in subsequent years.

3. In March 1946, as a preliminary step in carrying out the chartering objectives of the 1946 Act, Maritime (the War Shipping Administration) entered into short term bareboat charters with established steamship companies under the emergency wartime provisions of Public Law 101,[5] pending the fixing of sales

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[4] Emphasis supplied in all quotations unless otherwise indicated.

[5] Public Law 101 (Act of June 6, 1941, c. 174, § 3; 55 Stat. 243; 50 U.S.C. App. § 1273(a)) permitted chartering by WSA:

> upon such terms and conditions, for such period or periods, and subject to such restrictions as the Commission [WSA] may deem necessary or desirable for the protection of the public interest, and at such rate of hire as it may deem to be fair and reasonable. . . .

prices for vessels and the issuance of regulations and charter terms under the 1946 Act.[6] The terms of the interim charters (see foldout sheet attached hereto) were modeled after section 5 of the 1946 Act, and thus provided for a "basic charter hire" of 15 percent of the proposed sales price and for "additional charter hire [equal to 50 percent of profits] payable in accordance with the provisions of Sec. 709, Merchant Marine Act, 1936. . . ." (R. 76).

4. In mid-August 1946, Maritime adopted the standard form of Ship Sales Act charter (called "SHIPSALESDEMISE 303"). Petitioners (a nonsubsidized company) signed one of these charters on October 1, 1946, and operated ten Liberty-type vessels during 1946 and 1947 carrying bulk cargoes, primarily coal, in the coastwise and transatlantic trades. In this charter, the "basic charter hire" rate was fixed pursuant to section 5(b), *supra*, at 15 percent per annum of the "unadjusted" statutory sales price of the vessels. This figure was higher than that adopted for the interim charters and was, for most of the Liberty vessels of the type chartered by petitioners, about $14,000 per annum higher than the minimum authorized by section 5(b).[7] In fixing the profit sharing or

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[6] Section 5(a) of the 1946 Act (50 U.S.C. App. § 1738(a)) provided:

> No vessel shall be chartered under this section until sixty days after publication of the applicable prewar domestic cost in the Federal Register under subsection 3(c) of this Act.

[7] Section 3(d) of the Ship Sales Act (50 U.S.C. App. § 1736(d)) provided for the fixing of a "statutory sales price," for each type of vessel, for a downward adjustment in that price of 5 percent depreciation per year up to the date of sale or charter, and for a "floor" price below which no depreciation would be deducted. In the case of Liberty-type vessels chartered by petitioners, the "statutory sales price" was $639,000, and the "floor" price, $544,506

"additional charter hire" referred to in section 709(a), *supra*, Maritime, however, rewrote section 709(a) to substitute sliding scale rates of 50, 75 and 90 percent for the 50 percent specified in the statute. (See fold-out sheet)

5. The charterers individually and through industry associations protested the sliding scale of "additional charter hire" because it conflicted with the 50 percent rate set by section 709(a).[8] Following these protests, but before execution of the charters, Maritime added a clause which provided that payments of hire would be preliminary and subject to later adjustment.[9] Mari-

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(46 C.F.R. 299.89). The minimum basic charter hire permitted by section 5(b) of the Act was 15 percent of the "floor" price, or $81,675.90. This was, for most of the vessels chartered by petitioners, the depreciated price, or adjusted price "computed as of the date of the charter" referred to in section 5(b). The rate adopted by Maritime in August 1946 for the Ship Sales Act charters was 15 percent per annum of the unadjusted "statutory sales price" of $639,000, or $95,850. Thus, the basic rate was $14,174.10 per annum in excess of the minimum authorized by section 5(b). The rate charged in the interim charter was $87,424.95 per annum (R. 76).

[8] The industry protests and the amendment of the charters to reserve the charterers' rights are summarized in the *en banc* decision of the Court of Appeals for the Second Circuit in *American-Foreign Steamship Corp.* v. *United States*, 291 F. 2d 598, *cert. denied*, 368 U.S. 895 (1961). See especially the majority opinion of Judge Smith, 291 F. 2d at 602, and the dissent of Judges Friendly and Moore, *id.* at 613-15. These protests and reservations were also noted in *American Mail Line, Ltd.* v. *United States*, 213 F. Supp. 152, 155-57 (W.D. Wash. 1962), and *American President Lines, Ltd.* v. *United States* (N.D. Cal. 1963) (A1-A15). See also ftns. 43-45, *infra*, pp. 38-39.

[9] Clause 13—*Additional Charter Hire.*

* * *

The Charterer agrees to make preliminary payments to the Owner on account of such additional charter hire and on ac-

time also issued regulations which provided that the making of payments would not "prejudice the rights of either [party] under the applicable bareboat charter agreement or otherwise," and that if any charter provision was inconsistent with statute, the statute would govern.[10]

6. Both the interim and SHIPSALESDEMISE forms of charter restricted the routes on which the vessels might be operated and the cargoes which might be carried (R. 89). Maritime also issued regulations and instructions placing limitations on the freight rates charged to shippers and required that copies of all subcharters and contracts of affreightment be approved in advance of loading of cargo (R. 77-96).

7. In general, the charterers, including petitioners, sustained losses in late 1946 from the operation of vessels under the charters. On voyages during the first part of 1947, some of them made profits sufficient to require profit sharing payments in excess of 50 per-

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count of any additional charter hire accrued under any War Shipping Administration Form 203 (WARSHIPDEMISE-OUT) charter (prior to the times of payment provided for above or in such WARSHIPDEMISEOUT charters) at such times and in such manner and amounts as may be required by the Owner; provided however, that such payment of additional charter hire shall be deemed to be preliminary and subject to adjustment either at the time of the rendition of preliminary statements or upon the completion of each final audit by the Owner, at which times such payments will be made to the Owner as such preliminary statements or final audit may show to be due, or such overpayments refunded to the Charterer as may be required. (R. 183-84)

[10] Foldout sheet, quoting 46 C.F.R. §§ 299.31(k) and 299.56 (b)(5); also 46 C.F.R. § 299.39(a) and (b); 46 C.F.R. § 299.40(c); R. 98-106.

cent. The charter market then declined, and Maritime, concerned about losing its excessive shares of profits accrued up to that time, notified the charterers, including petitioners, on August 15, 1947, that their charters would be terminated as of September 1, 1947, but would be extended on condition that the charterers agree that losses from voyages after September 1 be accounted for separately from the profits on voyages commenced before that time.[11] Petitioners executed an addendum to the charter (called the "Foreign Trade Addendum") providing for this split acounting in 1947, such execution being subject to the reservation of rights, etc., described above in paragraph 5.

8. The effect, in petitioners' case, of the sliding scale and split year accounting was to allocate to the Government $516,000 of profits for the period prior to September 1, 1947, and to petitioners $196,000 for that period after allowable return. For the period after September 1, 1947, however, the vessels operated at a loss of $246,000 which was borne by petitioners but, because of the divided accounting requirement, did not reduce the share of profits allocable to the Government for the pre-September 1 period. The net result was that petitioners, on Maritime's accounting basis, will suffer a loss of $50,000 under the charter, while the Government will receive $1,223,000, consisting of $516,000 out of the profits for the first eight months of 1947 and

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[11] Maritime's reason for threatening to terminate the charters is recited in its annual report to Congress for the fiscal year ended June 30, 1948, as follows:

> This action was designed to require the charterer to carry on all operations after August 31, 1947, without offsetting future losses against additional charter hire due the Government, from voyage profits for the prior period. . . . (pp. 13-14)

$707,000 of basic charter hire paid to Maritime over the period of the charter (R. 109, 115).[12]

THE PROCEEDINGS BELOW

After the "final audit" of profits and losses from operations, petitioners brought an action under the reservation of rights clause of the charter and the applicable regulations to recover hire overpaid under the statute, and the Government counterclaimed for the amount withheld by petitioners because of these disputes.

The court below decided both the sliding scale and split accounting issues in favor of the Government, and affirmed the judgment of the district court against petitioners for the profit sharing hire which had been withheld. The court found in substance that the dominant purpose of the 1946 Act was to sell vessels, not to charter them, and that "the important consideration was to avoid making charters too cheap." (R. 258) It thus construed subsection (c) of section 5 (incorporating section 709(a)) as merely fixing a minimum profit sharing formula in favor of the Government, and found that the profit sharing percentages in excess of 50 percent were authorized by the general charter hire provisions of subsection (b) of section 5 of the 1946 Act, *supra*, which authorized charter hire "consistent with the policies of this Act. . ."

The court held that it was immaterial that Maritime had relied upon section 709(a) in fixing the profit sharing charges in excess of 50 percent since the power to increase the profit sharing hire existed in section

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[12] Petitioners' loss was partially reduced as a result of the compromise during the litigation of a collateral accounting claim under the charter (R. 30).

5(b). It found such misreliance to be merely a matter of form and not substance, and held that petitioners' contention was based upon a mere technicality. The court also upheld the split accounting requirement by similar reasoning.

SUMMARY OF ARGUMENT

Petitioners contend that the excess profit sharing provisions were not authorized by subsection (b) of section 5, because subsection (c) of the same section, incorporating section 709(a), set the profit sharing formula and limited the Government's share to 50 percent. The plain language of subsection (b) makes it clear that Congress authorized Maritime to establish thereunder only a fixed annual rate of hire based upon the statutory sales prices of the vessels. The equally plain and mandatory language of subsection (c) (incorporating section 709(a)) constituted an express limitation upon the power granted to Maritime by subsection (b), compelling the conclusion that Congress did not give Maritime discretion to change the profit sharing formula.

The record shows that Maritime adopted a fixed rate under section 5(b) of 15 percent, but modified the fifty-fifty profit sharing provisions of section 709 (a) without statutory authority because it thought that the Government should receive a greater share of the profits than that section provided. Since Maritime did not intend to fix the sliding scale excess shares under subsection (b) of section 5, the retroactive invocation of that subsection by the court below to validate the charge constitutes improper judicial reconstruction of agency action which has no foundation either in law or fact.

With respect to the divided accounting during the year 1947, petitioners contend that this requirement equally conflicts with the mandate of section 709(a) for "calendar year" accounting of "cumulative" profits. The record of Maritime's action in this respect shows that no bona fide termination of the charters was sought by the attempted cancellation in mid-1947 because, simultaneously with notice of termination, Maritime offered to continue the charters on condition that the charterers execute an amendment agreeing to the divided year accounting. This was done to circumvent the calendar year accounting plan of the statute and was accordingly invalid. The result was to permit the Government to retain its excessive shares of profits for the profitable portion of the year 1947 and to cast all of the losses thereafter upon the steamship industry, while the payment of basic charter hire continued as before.

ARGUMENT

I. THE PROFIT SHARING PERCENTAGES IN EXCESS OF 50 PERCENT WERE NOT AUTHORIZED BY SECTION 5 OF THE MERCHANT SHIP SALES ACT OF 1946

A. The Statutory Language is Clear and Unambiguous in Fixing Profit Sharing at 50 Percent

It is not necessary to go beyond the explicit language of section 5 to establish that the sliding scale exceeded the statutory authority conferred upon Maritime by Congress with respect to the fixing of bareboat charter terms.

The language of subsection (b) of section 5, *supra*, p. 4, is consistent only with the conclusion that it authorizes a fixed annual charter rate based upon a percentage of the statutory sales price of the vessels to be chartered. That subsection speaks of charter

hire to be "*fixed* by the Commission at such *rate* as the Commission determines to be consistent with the policies of this Act, but, except upon the affirmative vote of not less than four members of the Commission, *such rate* shall not be less than 15 per centum per annum of the statutory sales price (computed as of the date of charter). . . ." If a lower rate were found justified by four of the members it must be "not less than the *prevailing world market charter rate for similar vessels for similar use . . .*"

A profit sharing arrangement does not qualify as a "rate" of bareboat charter hire nor as a "world market charter rate" in any normally accepted sense. Profit sharing is neither fixed, ascertainable, nor predictable within the contemplation of subsection (b), because it is contingent and could result in no payment of hire if there were no profit. And the most conclusive evidence that subsection (b) of section 5 was not intended to authorize a profit sharing plan is the fact that in subsection (c) of the same section Congress incorporated the mandatory profit sharing plan of section 709(a).[13]

Furthermore, while subsection (b) authorized Maritime to fix rates "consistent with the policies of this Act," that language is followed by several express limitations on Maritime's power. Maritime could not under that section validly make a determination that a 90

[13] The terms of section 709(a) were brought to the attention of Congress both in the debates and in the reports on the legislation. See 91 Cong. Rec. 11877 (Dec. 12, 1945), where the complete text of the section was read in the Senate. The section was also referred to in H.R. Rep. No. 831, 79th Cong., 1st Sess. p. 9 (1945), and in S. Rep. No. 807, 79th Cong., 1st Sess. pp. 13-14 (1945). See Appendix B, legislative history, pp. B10, B11-12.

percent profit sharing rate was "consistent" when another provision of the same section made mandatory a 50 percent rate. Certainly, it could not be argued that a basic rate of less than 15 percent (without the concurrence of four members of Maritime) would be "consistent" with the policies of the act. The 50 percent profit sharing formula is no less a "policy" of the act than the minimum 15 percent basic rate. Indeed, it is a fixed term of the act.

Thus, because of the limitations in section 5, including the incorporation of section 709(a), the only determination which Maritime was authorized to make under subsection (b) was one relating to a fixed rate of hire based upon the statutory sales price. Its determination was that this should be 15 percent of the unadjusted statutory sales price (R. 70-71). It considered, but decided against, increasing this basic rate because, as hereinafter shown, the increase would have been borne primarily by the Government.[14] Its determination to increase the profit sharing hire was reflected in its rewriting of section 709(a), and because of the mandatory character of that section that increase was not authorized.

The construction of the statute by the court below, interpreting subsection (c) (incorporating section 709(a)) as prescribing a minimum only, reads into the statute the words "not less than" which are not there. The court below conceded that these words had to be supplied by implication (R. 255, 312 F. 2d at 220). As was pointed out in *American President Lines, Ltd.* v. *United States* (Appendix A), Congress employed the words "not less than" twice in subsection (b) of

[14] Infra, p. 36.

section 5 and knew their significance.[15] That court said (A6):

> To hold that the words "shall pay over to the Commission . . . one-half of . . . cumulative net voyage profit" means that the cumulative net voyage profit to be paid *shall not be less than* one-half thereof is judicial enactment into the statute of a concept and words which are not there. It cannot reasonably be contended that Congress did not know how to specify a minimum when it so intended. It did that very thing in this very statute by the requirements, in Section 5(b), that the charter rate "shall not be less than" 15 percent of statutory sales price except upon the affirmative vote of "not less than four members of the Commission" as well as by the requirement therein that the charter rate under certain circumstances "shall not be less than" the referenced prevailing world market rates. (Emphasis by the court)

While both sections 5(b) and 709(a) contain the words "charter hire," it is not difficult to perceive that they have different objectives and involve entirely different basic economic concepts to the charterer. Section 5(b) contemplates an annual fixed hire based upon a percentage of purchase price, an expense of operation payable irrespective of profits and loses. Section 709(a), on the other hand, defines "additional charter hire" and embodies a unique profit sharing arrangement not present in the normal charter. It is based upon a percentage of cumulative profits after deduction of the annual fixed hire, overhead expense and return on capital. The percentages referred to have no common base. The court below disregarded

[15] See legislative history, Appendix B, p. B13, for other sections of the 1946 Act using the words "not less than."

these different concepts in holding that subsection (b) of section 5 authorized the same type of arrangement as subsection (c). The actions taken by Maritime recognized this difference in concept, and it dealt separately with the fixed hire rate and with the profit sharing formula (R. 70-71).

Even if there were some ambiguity in the statutory language, there are several well-settled rules of statutory construction which compel the construction urged by petitioners. These rules were rejected by the court below in favor of the exceptions to the rules. One is that where two sections of the same statute are by their terms applicable to related subject matter, and one (section 709(a)) is specific, and the other (section 5(b)) is general, the specific provision controls to the exclusion of the general, particularly where, as so construed, conflict is avoided between the two sections.[16] Here, section 5(b) is applicable to the general subject of a fixed rate of "charter hire," which must "not be less than 15 per centum per annum of the statutory sales price." Section 709(a) is applicable, to use its own terminology, to profit sharing defined as "additional charter hire." Since this is the specific provision with respect to profit sharing, it controls that feature of the charter to the exclusion of the general "charter hire" provision of section 5(b).

A companion rule is that where a statute directs a government agency to act in a specific manner, that

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[16] *Bulova Watch Co.* v. *United States*, 365 U.S. 753, 759 (1961), and the cases cited therein; *United States* v. *Moran*, 236 F. 2d 361, 363 (2d Cir. 1956), *cert. denied*, 352 U.S. 909 (1956); and *State Mutual Life Assur. Co.* v. *Commissioner*, 246 F. 2d 319, 323 (1st Cir. 1957).

direction includes a mandatory negative.[17] The mandatory language of section 709(a) shows it to be a maximum and minimum and negates the existence of discretion under 5(b) to change the profit sharing formula in any respect.

Finally, section 5 should be construed in such a way as to give effect to all of its parts, and any construction which creates a conflict or renders any part of the statute superfluous must be avoided. If Congress wished to give Maritime unfettered discretion to appropriate the charterers' profits, there was no need for section 709(a). The interpretation of the statutes adopted by the court below renders section 5(c) (incorporating section 709(a)) not only superfluous, but also incompatible with section 5(b), whereas the position of petitioners gives effect to both sections.[18]

B. The Weight of Well-Reasoned Authority Supports Petitioners

Nine decisions have been written dealing with the sliding scale profit sharing provisions contained in the Ship Sales Act form of charter. Four of these

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[17] *Botany Worsted Mills* v. *United States*, 278 U.S. 282, 289 (1929); *Raleigh and Gaston R.R. Co.* v. *Reid*, 80 U.S. (13 Wall.) 269 (1872); *McIlhenny* v. *Commissioner*, 39 F. 2d 356, 358, (3d Cir. 1930); *United States* v. *Gutzler*, 105 F. 2d 188 (9th Cir. 1939); *Jones* v. *H.D. & J.K. Crosswell*, 60 F. 2d 827 (4th Cir. 1932); *cf. Sword Line* v. *United States*, 228 F. 2d 344, 346 (2d Cir. 1955).

[18] *Washington Market Co.* v. *Hoffman*, 101 U.S. 112, 133 (1879); *United States* v. *Menasche*, 348 U.S. 528, 538-39 (1955); *Jarecki* v. *Searle & Co.*, 367 U.S. 303 (1961); *Ex parte Public Nat. Bank*, 278 U.S. 101, 104 (1928). The foregoing principle was applied in construing section 709(a) in *United States* v. *Moore-McCormack Lines, Inc.*, 308 F. 2d 866, 871, 874 (4th Cir. 1962), *cert. denied*, 372 U.S. 944 (1963).

squarely support petitioner's position,[19] two tend to support it,[20] and three reject it.[21]

The first decision supporting petitioners was *Dichmann, Wright & Pugh, Inc.* v. *United States* (*"Dichmann"*), 144 F. Supp. 922, 925 (S.D.N.Y. 1956), in which Judge Dimock concluded that the Government's share of profits was limited by subsection (c) of section 5 (incorporating section 709(a)) to 50 percent and that the sliding scale portion could not be justified under the more general provisions of subsection (b), as follows:

> To substantiate such an expansion of the literal meaning of the statute and of its original intent, the owner invokes the power given to the Commission by section 5(b) to fix the charter hire rate. That power, however, was exhausted when the amount of the charter hire was fixed. That amount was fixed in dollars "at such rate as the Commission determines to be consistent with the policies of this Act". To say that the power to fix the charter hire carries over to the fixing of the

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[19] *Dichmann, Wright & Pugh, Inc.* v. *United States*, 144 F. Supp. 922 (S.D.N.Y. 1956); *American Export Lines, Inc.* v. *United States*, 290 F. 2d 925 (Ct. Cl. 1961); *American Mail Line, Ltd.* v. *United States*, 213 F. Supp. 152 (W.D. Wash. 1962); *American President Lines, Ltd.* v. *United States* (N.D. Cal. Oct. 10, 1963, unreported, Appendix A, pp. A1-A15).

[20] *Sword Line* v. *United States*, 228 F. 2d 344, *aff'd*, 230 F. 2d 75 (2d Cir. 1955), *aff'd as to admiralty jurisdiction*, 351 U.S. 976 (1956); *United States* v. *East Harbor Trading Corp.*, 190 F. Supp. 245 (S.D.N.Y. 1960).

[21] The district court below (R. 5-33), 202 F. Supp. 297, supplemental opinion, 210 F. Supp. 822 (D. Mass. 1962), and the court of appeals below (R. 247-60), 312 F. 2d 214 (1st Cir. 1963); *United States* v. *Eastport Steamship Corp.*, 216 F. Supp. 649 (S.D.N.Y. 1963, appeal argued November 21, 1963).

rate of division of the excess profits under 709(a) would be to render the statutory scheme for two items of charter hire meaningless. The effect of the rule contended for by the owner is that the Commission could fix the rate of the owner's share of the excess profits at any figure not less than 50% so long as the net result would be that the sum of the "charter hire reserved in the charter" and the "additional charter hire" would produce "such rate as the Commission determines to be consistent with the policies of this Act". If the entire amount payable under the charter party were indeed to be nothing but charter hire "at such rate as the Commission determines to be consistent with the policies of this Act," no intelligible purpose could be assigned to a statutory requirement that this amount be expressed in the charter party as the sum of an arbitrarily fixed "charter hire reserved in the charter" and an "additional charter hire" developed from the "charter hire reserved in the charter" among other factors.

The *Dichmann* reasoning was followed by the Court of Claims in *American Export Lines, Inc.* v. *United States* (*"American Export"*), 290 F. 2d 925, 930-31 (1961):

> We think it is clear that under the provision quoted above, the Commission was without authority to raise or lower the 50 percent of the excess profits which plaintiffs were required to pay as additional charter hire. This 50 percent share is a maximum as well as a minimum, at least insofar as section 709(a) is concerned. Dichman, Wright & Pugh, Inc. v. United States, supra; United States v. East Harbor Trading Corp., supra. That it was intended for the charterer to share fifty-fifty, no more and no less, is clearly apparent from the language of the statute.

> However, defendant argues that the sliding scale for payment of profit in excess of 50 percent was inserted in the charter contracts pursuant to its authority under section 5(b) of the Merchant Ship Sales Act of 1946, supra, to fix a rate of basic charter hire "consistent with the policies of this Act."
>
> This is contrary to the provisions of the charters. . . .
>
> * * *
>
> It [the charter] specifically provided for a basic rate of 15 percent, and such a rate was specifically authorized by statute. What was unauthorized by statute was the additional hire in excess of 50 percent.
>
> The following cases are in accord: Dichman, Wright & Pugh, Inc. v. United States, supra; United States v. East Harbor Trading Corp., supra. The power to fix the basic charter hire rate under section 5(b) was exhausted when the 15 percent rate was fixed by the contracts. It would appear that defendant's theory, that the sliding scale of from 25 to 40 percent of the excess profit constituted a portion of the section 5(b) basic rate, was an afterthought and not in the minds of the parties when the contracts were entered into.
>
> We are of the opinion that defendant had no authority to charge any amount as additional charter hire in excess of 50 percent of the cumulative net voyage profits.

In *American Mail Line, Ltd.* v. *United States* (*"American Mail Line"*), 213 F. Supp. 152, 163 (W.D. Wash. 1962, appeal pending), the court followed the holdings in *Dichmann and American Export, supra.* It further held that the Government could not properly rely on an administrative determination which Mari-

time had never made under section 5(b) to support the sliding scale charge actually made under section 709(a), even if it be assumed that such a determination were permissible under the former section.[22]

The most recent decision on the sliding scale issue is *American President Lines, Ltd. v. United States* ("*American President Lines*") (N.D. Cal., Oct. 10, 1963, Appendix A, pp. A1-A15). The court there concluded that the sliding scale was clearly contrary to the governing statutory provisions, stating (A4-A6):

> Section 5(b) begins by authorizing the Commission to fix charter hire "at such rate as the Commission determines to be consistent with the policies of this Act . . .". This grant of authority is then limited in three respects.
>
> The first limitation is that the rate of charter hire shall not be less than 15 per centum per annum of the statutory sales price, computed as of the date of charter, except upon the affirmative vote of no less than four members of the Commission. This limitation, contained in the first sentence of 5(b), is not involved in this case because the charter here requires a hire of at least the 15 percent requisite to avoid application of the limitation.
>
> The second limitation is to the effect that the rates of charter hire fixed by the Commission shall, if they "differ from the rate specified," not be less than the prevailing world market charter rates. This limitation, set out in the second sentence of 5(b), is not here involved because the rate provided in the charter does not so differ.
>
> The third limitation stems from the statutory declaration of Section 5(c) requiring that the pro-

[22] The court relied on *Bell* v. *United States*, 366 U.S. 393, 412 (1961). This and other similar cases are discussed *infra* pp. 41-42.

visions of Section 709(a) "*shall* be applicable to charters made under" Section 5(b) (emphasis added). The charter here is undeniably one made under Section 5(b). No one has suggested that there is any other authority for it, and there is none. It is plain, therefore, that the provisions of 709(a) apply. Congress could hardly have used language more clearly so requiring.

It is perhaps worthy of note here that, while the first two limitations upon the authority granted the Commission are stated as exceptions, the limitation imposed by Section 5(c) is stated positively and affirmatively through employment of the command "shall". It would hardly seem appropriate to treat a positive command as having less force in specifying a qualification upon a grant of power than a statement or statements qualifying that grant in the form of exceptions.

What, then, is the limitation upon the authority of the Commission thus made applicable by explicit command? It is a declaration in 709(a) which spells out in detail those provisions which must be included in "*Every charter made by the Commission* pursuant to the provisions of this title . . ." (emphasis added). When examination is made of the provisions which Congress had thus declared requisite to every charter made by the Commission, we find an unambiguous, carefully worded and easily understood statement that every charter shall provide that "the charterer shall pay over to the Commission, as additional charter hire, one-half of such cumulative net voyage profit in excess of 10 per centum per annum . . .". Congress was careful and exact in its designations in 709(a) as to what it meant by the terms used in the quoted phrase.

The two decisions which are not direct holdings but which tend to support petitioners' position are *Sword*

Line v. *United States*, 228 F. 2d 344, *aff'd*, 230 F. 2d 75 (2d Cir. 1955), *aff'd as to admiralty jurisdiction*, 351 U.S. 976 (1956), and *United States* v. *East Harbor Trading Corp.*, 190 F. Supp. 245 (S.D.N.Y. 1960).

In *Sword Line*, Judge Learned Hand, in dealing with the jurisdiction question, said (228 F. 2d at 346):

> On the other hand, if the statute [section 709(a)] did indeed limit the Commission to an even division of profits, it was the Commission's duty so to limit the libellant's promise; and we should not assume that the Commission would not have chartered the ships, unless it was to receive the unlawful hire. Obviously, we may impute to the libellant willingness to pay the lesser hire; so that it is proper to proceed as though there had been a contract for an even division, and nevertheless the Commission had compelled the libellant to pay more than the disputed hire. . . .

In *East Harbor*, Judge Kaufman said, with respect to section 709(a), (190 F. Supp. at 249):

> It is apparent that this section not only authorized, but required the parties to insert a provision in the charter for payment by the charterer of 50% of his profits to the government. And, as Judge Dimock held in Dichman, Wright & Pugh, Inc. v. United States, supra, this 50% share is a maximum as well as a minimum, at least insofar as section 709 is concerned. Cf. Sword Line, Inc. v. United States, 2 Cir., 1955, 228 F. 2d 344. Therefore, there is clearly no authority conferred by section 709 for the inclusion of that portion of the charter clause requiring payments in excess of 50% of profits.

The record before Judge Kaufman did not contain the minutes, memoranda, etc., of Maritime, but he was

of the opinion that if they showed that Maritime had relied on section 5(b) in fixing the excess portions of additional charter hire, the Government might be entitled to recover, but that if they showed that the charge was made under 709(a), it might not recover, stating (190 F. Supp. at 249):

> If, however, the parties mistakenly believed that authorization for the sliding scale could be found within section 709(a), and inserted this clause pursuant to that section, the defendant [steamship company] must prevail.

The minutes, etc., of Maritime show[23] that the excess charge was in fact made in reliance upon section 709 (a), and it may, therefore, be concluded that Judge Kaufman's decision would be that the sliding scale charges were contrary to the relevant statutes.

The three decisions upholding the legality of the sliding scale are those of the district court and court of appeals below, and *United States* v. *Eastport Steamship Corp.* (*"Eastport"*), 216 F. Supp. 649 (S.D.N.Y. 1963, appeal pending). Each of these decisions holds that section 5(c), incorporating section 709(a), fixed a minimum profit sharing formula only, and that the excess sliding scale charges were authorized by section 5(b). They accept the fact that Maritime purported to rely upon section 709(a) in fixing the sliding scale, but hold that such reliance was a matter of form and

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[23] See the discussion infra pp. 37-38, and the regulations and charter provisions on the foldout sheet attached hereto. Maritime's memoranda, minutes and telegrams to the charterers repeatedly identify the "basic charter hire" of 15 percent with section 5(b). They refer to the profit sharing hire, including the sliding scale portions, as "additional charter hire" following the language of section 709(a).

not substance, because it could have reached the same result if it had relied upon section 5(b).

The decisions are unanimous in holding that contract provisions purporting to modify the mandatory terms of the Merchant Ship Sales Act of 1946 are ineffective, and that the statutory terms prevail over and are substituted for the inconsistent contract terms. In addition to the cases cited above, see *United States* v. *Moore-McCormack Lines, Inc., supra,* 308 F. 2d 866, 873-74 (4th Cir. 1962), *cert. denied,* 372 U.S. 944 (1963); *Southeastern Oil Florida* v. *United States,* 119 F. Supp. 731, 734-35 (Ct. Cl. 1953), *cert. denied,* 348 U.S. 834 (1954); *A. H. Bull Steamship Co.* v. *United States,* 108 F. Supp. 95, 99 (Ct. Cl. 1952); *Nautilus Shipping Corporation* v. *United States,* 158 F. Supp. 353, 354-55 (Ct. Cl. 1958).[24] This principle applies whether or not there is a protest, and whether or not the right to contest the unlawful contract provision is reserved. In this case, however, there was both a protest and an express reservation.

C. The Legislative History Demonstrates That the Profit Sharing Plan Was Mandatory and That Section 709(a) Fixed Both a Floor and Ceiling in the 1946 Act

The court below recognized that section 709(a) fixed both a floor and a ceiling for purposes of the Merchant Marine Act, 1936 (R. 255, 312 F. 2d at 220), but it found that for purposes of the Merchant Ship Sales Act of

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[24] These cases also dispose of the contention of the Government that if the sliding scale is found to violate section 5, all of the charter terms are nullified and the parties are relegated to a *quantum valebat* situation under which the court may fix the reasonable value of the vessels. (See also 46 C.F.R. § 299.56(b)(5), quoted on the foldout sheet)

1946 the same section merely fixed a floor.[25] In reaching this conclusion, it recognized that there was no direct evidence (R. 257, 312 F. 2d at 221) of the intent of Congress in this respect, and it reached its conclusion for the reasons, first, that the 1946 Act showed a policy to prefer sales over charters, and, second, because the 1946 Act substituted negotiation of rates of charter hire for the competitive bid procedure contained in the 1936 Act. Neither of these reasons is sound, because the legislative history shows that both acts preferred the sale of vessels over charter (but both authorized chartering in broad terms) and both acts (not just the 1946 Act) contained provisions for the negotiation of charter hire rates.

The provisions of the 1936 and 1946 Acts relating to sale and charter of vessels are closely parallel. Each act commences with a substantially identical statement of policy: to develop and expand the merchant marine in private hands. (1936 Act, 46 U.S.C. § 1101; 1946 Act, 50 U.S.C. App. § 1735) Each authorizes a minimum rate of charter hire of "not less than" a fixed percentage of a selling price independently established. Section 714 of the 1936 Act (46 U.S.C. § 1204) provides that if essential trade routes cannot otherwise be successfully developed, Maritime may construct vessels and bareboat charter them to private steamship companies at negotiated rates "upon an annual charter hire of not less than 5 per centum of the price . . . plus 3½ per centum of the depreciated foreign cost com-

[25] The legislative history of the chartering provisions of the 1936 Act, confirming that a minimum and maximum profit sharing formula of 50 percent was contemplated, is contained in Appendix B, pp. B1-B9.

puted annually . . .'"[26] Section 5 of the 1946 Act (50 U.S.C. App. § 1738) provides for chartering at "not . . . less than 15 per centum per annum of the statutory sales price (computed as of the date of charter)." Under each act, section 709(a) was made a mandatory clause in the charters. (1936 Act, 46 U.S.C. § 1199(a); 1946 Act, 50 U.S.C. App. § 1738(c)) Thus if the decision of the court below is affirmed, Maritime will apparently be authorized under section 714 of the 1936 Act, to increase the profit sharing percentages fixed by section 709(a) in charters made in the future under that act.

By including the chartering provisions, Congress obviously recognized the importance of chartering in reconstruction of the private merchant marine. There are many comments in the legislative history as to the desirability of chartering, just as there are to the matter of preferring sales to charters (B9-B12). Section 7(a) (*supra* ftn. 3 p. 4) directed Maritime to prefer sales over charters only *"so far as practicable."* This does not reflect an inflexible or overriding policy. Furthermore, the safeguards which Congress thought adequate to prefer sales to charters were written specifically into the act. Section 5(a) of the act (50 U.S.C. App. § 1738(a)) provided that no vessel should be chartered until sixty days after Maritime had published the applicable sales price in order that purchasers might during that sixty day period select vessels for purchase before they were made available for charter.

Finally, the legislative history of the 1946 Act shows that the 15 percent rate adopted by Congress was

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[26] The 8½ percent floor was reduced to 7½ percent in June 1960. (See 46 U.S.C.A. § 1204, Annotations)

recognized to be a high rate, which in itself would discourage chartering and encourage sales.[27] The bareboat charter rate first proposed to Congress for the 1946 Act was not less than 8½ percent of the sales price, this percentage being the minimum set by section 714 of the 1936 Act, discussed *infra* p. 26.[28] Maritime later recommended to Congress that this be increased to 12½ percent.[29] As finally enacted, basic charter hire was fixed at "not less than 15 percent" of the adjusted statutory sales price. In discussing the 15 percent rate, Senator Radcliffe, who was in charge of the bill which became the Ship Sales Act, stated (91 Cong. Rec. 11873 (1945)):

> If the Government collects 15 percent for several years, the Senator can readily see that would be rather a substantial amount. The general opinion of those who have given this matter careful consideration is that the *15 percent is such a high rate that it will have rather a discouraging effect upon chartering rather than buying, and that runs all through the bill.*

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[27] The 15 percent rate was composed of 5 percent depreciation, 3½ percent interest, and 6½ percent profit to the Government, based upon the respective sales prices of the vessels chartered. (S. Rep. No. 807, 79th Cong., 1st Sess. pp. 13-14 (1945)) The profit portion of the hire for a Liberty-type vessel was, therefore, 6½ percent of $639,000, or $41,535 of the $95,850 annual basic charter hire. The 15 percent rate would return to the Government the full statutory sale price of a Liberty-type vessel if chartered for about six and two-thirds years, and the "floor" price in five and two-thirds years.

[28] See H. R. 4486, 78th Cong., 2d Sess. (1944) § 1(c).

[29] Hearings before the House Committee on Merchant Marine and Fisheries on H. R. 1425, 79th Cong., 1st Sess. pp. 452, 455 (March, 1945).

The following colloquy then ensued (*ibid.*):

> Mr. Hill. If they had to pay 15 percent for every year the ship was chartered, it might be we would get more for chartering a ship, if the charter were to run for several years, than if we sold the ship.
>
> Mr. Radcliffe. That is entirely true, and *that is one reason why we fixed the rate fairly high*, . . .

Senator Magnuson also made the following statement (91 Cong. Rec. 11552 (1945)):

> I do not think we are giving away anything. *I think a charter price of 15 percent is rather high*, . . .

Furthermore, the legislative history shows that Congress was concerned that the 15 percent rate was too high and that it would unduly restrict chartering. It therefore added the last sentence to section 5(b) to permit a lower rate of hire. The Senate report[30] on the Ship Sales Act stated:

> This rate of 15 percent conforms with the wartime practice of fixing bareboat use under War Shipping Administration operation at 15 percent of value for vessels built since 1937—a standard generally regarded as reasonable for the past . . . It is recognized that the value of the use may decline in the future because of the existence of tonnage in excess of world shipping requirements. *The Commission is given discretion by a vote of four to prescribe a lower rate*, subject to the limitation as to world charter rates.

The general policy of preferring sales over charters has not been regarded by any court other than the one

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[30] S. Rep. No. 807 (to accompany H. R. 3603), 79th Cong., 1st Sess. p. 14 (1945).

below to be sufficient grounds for reading the words "not less than" into the otherwise plain language of section 709(a). For example, in *American President Lines*, pp. A7-A8 the court said:

> Moreover, the requirement of equally dividing cumulative net voyage profit between the Commission and the charterer may well be advantageous to the government of the United States and serviceable to proper Congressional purposes. There are interlocking relationships between revenue from charter hire on the one hand and, on the other, costs of shipping, including costs of shipping which must be borne by governmental agencies. *While one purpose of the statute was to encourage sale over charter, there were other objectives calling for a balancing, such as, for example, encouragement of a thriving American Merchant Marine for the purposes of defense, full employment and the like.* The provisions of 709(a) requiring, in effect, that charterers should receive 50 percent of certain profits make good sense in that interest.

Problems encountered in the administration of the ocean mail contract subsidy program led Congress to restrict by most specific language the discretion of Maritime in the 1936 and 1946 Acts. Congress was asked by the Maritime spokesman to fix the principal financial terms to be included in the 1946 Act.[31] Sec-

[31] See the hearings before the Senate Committee on Commerce on S. 292, 79th Cong., 1st Sess. p. 98 (Sept. 14, 1945):

> Admiral Land. Yes; but we want to do it legislatively so there won't be any criticism, have the Congress put the ceiling and the floor. I am not looking for a Black investigation.
>
> Senator Brewster. You mean you don't trust yourself?
>
> Admiral Land. I don't trust myself nor my posterity. No, I certainly don't and all the history of maritime legislation going back to 1904 shows that we aren't worthy of being

tion 709(a) is an example of one of these specific terms.[32] It was the intention of Congress to circumscribe Maritime's discretion in order that the latter would be protected against pressures from the industry and from later accusations of favoritism; and, conversely, to protect the industry against arbitrary or discriminatory agency action.[33]

Under Maritime's bareboat charter, the charterer was required to pay basic charter hire, furnish and pay the crew, keep the vessel insured and in good repair, and redeliver it at the termination of the charter in the

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trusted, due to the conditions that arose, and that applies to the Congress as well as every man who was on this job before I was.

Senator Brewster. How is the Congress better able to do it, if you can't trust them?

Admiral Land. I do trust them. We give them the best information we have and they enact it, and then there won't be any investigation or any row with the Comptroller General or anybody else.

[32] See legislative history, Appendix B, pp. B12-B19.

[33] In *Nautilus Shipping Corporation* v. *United States*, 158 F. Supp. 353, 354-55 (Ct. Cl. 1958), the court said:

> The Merchant Ship Sales Act of 1946, *supra*, was an attempt on the part of Congress to provide for the sale of the Government's large accumulation of surplus ships at prices which could be calculated on the basis of a statutory formula. It was intended to relieve the Maritime Commission of the responsibility of haggling over prices, and of the criticism, embarrassment and possible scandal which might result if sales were individually negotiated. If that policy was to be carried out, the terms of the statute had to be adhered to, even though litigation might be necessary to determine the proper construction of a rather complex statute. That did not leave any room for individual bargaining for terms contrary to the statute, nor much room for the application of such doctrines as estoppel and acquiescence. . . .

See also *Sprague Steamship Co.* v. *United States*, 172 F. Supp. 674, 675 (Ct. Cl. 1958).

same good order and condition as when delivered, making allowances for ordinary wear and tear. The charterer also solicited the cargo, paid for loading and discharging, and directed the operations of the vessel. It assumed all risks of loss from the venture, including delays from labor difficulties, adverse weather conditions, congested ports, etc. Normally, the party bearing the risk of loss is entitled to retain all of the profits. Since Congress fixed a high basic rate of hire, there is no reasonable basis to assume that it meant to take away any more of the profits than section 709(a) clearly specified. Any interpretation which deprives the industry of the profits which it might use to expand the United States-flag merchant marine is clearly contrary to the statements of policy of both the 1936 and 1946 Acts.[34] The former act sought to build up a failing industry necessary for national defense, and the latter was designed to restore an industry torn by World War II.[35]

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[34] Section 101 of the Merchant Marine Act, 1936 (46 U.S.C. § 1101), and section 2(a) of the Merchant Ship Sales Act of 1946 (50 U.S.C. App. § 1735).

[35] The federal income tax laws similarly make the United States a participant in the profits of private industry, but no one would suggest that they should be construed to fix minimum rates, or to authorize the Internal Revenue Service to exact more than the statutory rates. In this connection, it should be pointed out that the 50 percent of profits retained by the charterers, as well as their 10 percent return on capital, are subject to income tax. Thus, in profit years the Government would effectively receive about 75 percent of the profits, even if section 709(a) fixed 50 percent as a maximum and minimum. If the profit sharing rate is 90 percent, the charterers' profits are minimal after income tax, and the incentive to expand shipping enterprises, develop trade routes, etc., is substantially undermined.

D. The Court Below Was in Error in Holding That Section 5(b) May Be Invoked Retroactively To Validate Unlawful Action Taken by Maritime in Reliance Upon Section 709(a)

Petitioners' primary contention is that the grant of authority to Maritime in subsection (b) of section 5 to fix charter rates was restricted by subsection (c) to a profit sharing provision containing the specific terms of section 709(a). Accordingly, the excess profit sharing provision would not have been valid even had Maritime purported to make an express finding under subsection (b) that such charge was "consistent with the policies of this Act, . . ." But, assuming for purposes of argument that a finding under subsection (b) might have been made, a review of the circumstances under which Maritime adopted the sliding scale demonstrates affirmatively that Maritime did not intend to fix the sliding scale excess shares under that subsection. It fixed them under 709(a), then rejected the protests of the industry that these shares were unlawful under that section, and made it clear by amendment to the charter and the issuance of regulations that the rights of the parties were reserved in respect of the dispute. The retroactive invocation of subsection (b) by the court below to validate the charge constitutes improper judicial reconstruction of agency action, which, as explained in the next point herein, adversely affects petitioners' substantive rights under the statute and the charter.

The records of Maritime show a clear understanding by that agency of the difference between the basic charter hire authorized by subsection (b) and the excess profit sharing charges fixed under subsection (c) incorporating section 709(a). In selecting the 15 percent rate as "consistent with the policies" of the act under subsection (b), several considerations were cited

by Maritime. Among these were (a) that declines were expected in the charter market because of competition by foreign-flag vessels being sold to noncitizens under the 1946 Act;[36] (b) that some types of vessels available for charter did not justify a rate in excess of 15 percent;[37] (c) that rates to shippers were controlled through conferences of American and foreign carriers whose rates were approved by Maritime;[38] (d) that

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[36] Memorandum to the Commission from the Acting Chief, Charter Section, dated August 7, 1946, entitled "Report on WSA Interim Chartering and Recommendations in Connection with Maritime Commission Chartering under the Ship Sales Act":

> With foreign nations having more tonnage available through sales of U. S. vessels, it is natural that rates will decline from the levels which have in the past necessarily been set by WSA for vessels operated by WSA whose expense of operation is greater than that for privately operated vessels. . . . (R. 48)

Minutes of the Maritime Commission dated August 9, 1946:

> Mr. Darr stated that with sales of ships being made to foreigners at a rapid rate the world market would be necessarily affected by low charter rates which foreign competitors have indicated will be placed in effect. . . . (R. 65-66)

[37] Report to the Commission of a Special Charter Committee dated August 8, 1946:

> The Committee is informed that there are certain types of "war-built" vessels available for charter that will not warrant a higher basic rate than 15% of the sales price. We also are informed that equitable basic rates in the various foreign trades will differ materially. . . . (R. 55)

[38] The August 7, 1946 report further states:

> The rates on general cargo carried by the berth services are practically all governed by the respective line group conferences, and while many of the berth services are highly profitable with the full cargoes and rates prevailing today, some berth services in some of the trades are not highly remunerative but are fraught with both operating risks and traffic risks. . . . (R. 49; see also R. 89-96)

since the Government had a monopoly on vessel tonnage it controlled world market charter rates through that monopoly;[39] and (e) that Maritime was able to control the level of rates through its power to approve in advance voyage charters and contracts of affreightment.[40]

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[39] As the court said in *American-Foreign* (291 F. 2d at 602):

> During the Second World War the United States Government, not surprisingly, had a virtual monopoly on the ownership of all floating vessels. . . .

The McDaniel affidavit states (R. 143):

> The committees on which I served began to realize that the United States, *having control of the great bulk of the world tonnage, also controlled the world market*, and that too low charter rates would permit undercutting on freight rates with extremely harmful results to pre-war American owners and post-war American vessel purchasers who were trying to establish themselves.

[40] A government affidavit filed in *Smith-Johnson Steamship Corp. v. United States*, 142 F. Supp. 367 (Ct. Cl. 1956) states:

> The Commission also approved the application of WSA Bareboat Charter Regulation No. 3 to Commission charters, with certain modifications. It was to continue to require the filing of voyage charters and contracts of affreightment with the Commission, the compliance with conference or WSA rates (except coal and grain rates established in WSA Bareboat Charter Regulation No. 1 and except full, bulk cargoes not hand stowed), the limiting of commissions, the refusal to charter additional vessels for 60 days after a redelivery with exception of redeliveries off berth for more suitable substitutions, and the limiting of sub-time chartering to that approved by the Commission "*at current market time charter rates* for American vessels as determined by the Director of Traffic," copies of the sub-time charters to be submitted for approval. . . . (Emphasis in original affidavit) (p. 57a)

A letter of award of a War Department charter made in circumstances substantially identical with petitioners' War Department charters (R. 39) was introduced as an exhibit in *American Export*

The record also reveals another important reason for Maritime's not wishing to act under subsection (b) of section 5 to increase the 15 percent basic hire in lieu of imposing the sliding scale rates. This was that such an increase would be passed on to the Government either by increases in rates for the movement of government cargoes, or under clauses in subcharters with other government agencies providing that any increase in the 15 percent basic rate would be paid by the government agencies concerned.[41]

Lines, Inc. v. *United States*, *supra*, 290 F. 2d 925 (Ct. Cl. 1961). It pointed out that these charters were made at rates less than the commercial market:

> The per diem rate of $1,515 while in port and $1,765 per day while at sea, was arrived at after consideration of operating costs determined after careful study by the Maritime Commission, this office, and examination of reports of various commercial operators. The formula and the rate arrived at have heretofore been approved by your office. *This office is in constant touch with brokers and operators and has formed its best judgment as to the commercial charter rates which are substantially higher than the rate contained in the proposed contract.*

[41] As Judge Beeks found in *American Mail Line* (213 F. Supp. at 162, ftn. 13):

> Maritime considered increasing the basic charter hire rate of 15 percent per annum of the statutory sales price but did not do so because of protests from other governmental agencies, the Army and the State Department. These agencies had subtime/voyage/space charters with various operators containing escalation clauses providing that if the operators' basic hire was increased by Maritime, the rate of hire specified in the subcharter would be adjusted accordingly.

Petitioners time chartered two of the vessels to the War Department under conditions which would require the latter to pay any increase in the basic 15 percent rate of hire (R. 39).

The McDaniel affidavit in *Smith-Johnson*, *supra*, states in part:

> Other Government agencies vigorously objected to the long-range plan. *The Army requested that no increase be made in*

Concerning the fixing of the profit sharing terms, the records of Maritime show a direct concern with and reliance upon the language of section 709(a).[42] The parallel language of the statute, regulations and charter provisions set forth on the foldout sheet shows that Maritime was not relying, and did not intend to rely, upon subsection (b) of section 5 in fixing the

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[the 15 percent] *basic charter hire* since Army appropriations for the fiscal years ending June 30, 147 [sic] and 1948 could not absorb such an increase under the clause in the Army's sub-time charters of vessels under the Form 303 charter to the effect that if the basic charter hire under the Form 303 charter is increased or decreased the rate of compensation specified in the Army subtime charters

will be adjusted in the amount that such basic charter hire is greater or less than 15 percent per annum on the estimated statutory sales price.

(See March 13, 1947, Helmbold to Commission; March 6, 1947, Chief of Army Transportation to Commission Chairman.)

The *State Department also demurred to the increase* for fear of resultant increases in freight rates, which, it was stated, then accounted for 26 percent of the value of the cargo carried (April 3, 1947, Commission minutes) . . . (p. 93a)

[42] Maritime's memoranda and minutes repeatedly refer to an increase in the rate of "additional charter hire," a term found only in section 709(a). See the August 8, 1946 memorandum (R. 56):

All of the Committee members, except one, agree that the *additional charter hire of 50% of the profits in excess of 10% of Capital necessarily employed in the business should be increased.* A minority of the Committee, however, feel that the revised percentage being recommended is too high.

A telegram to charterers was proposed, as follows (R. 63):

3. THE *ADDITIONAL CHARTER HIRE* PAYABLE TO THE OWNER WILL BE NINETY PERCENT OF THE NET VOYAGE PROFIT IN EXCESS OF THE TEN PERCENT PER ANNUM ON CHARTERER'S CAPITAL NECESSARILY EMPLOYED *INSTEAD OF FIFTY PERCENT* [IN THE INTERIM CHARTERS] *AS HERETOFORE.*

excess shares, but was merely increasing the profit sharing percentage contained in section 709(a).

These separate statutory determinations were reflected in the telegram by which the petitioners were notified of the charter terms, as follows (R. 204):

> 2. THE RATE OF BASIC HIRE WILL BE AT RATE OF FIFTEEN PER CENT PER ANNUM OF EITHER THE UNADJUSTED STATUTORY SALES PRICE OR THE FLOOR PRICE OF THE VESSEL, WHICHEVER IS HIGHER.
>
> 3. THE ADDITIONAL CHARTER HIRE PAYABLE UNDER AND DURING THE PERIOD OF THE FLEET CHARTER SHALL BE (a) 50 PER CENT OF THE AVERAGE NET VOYAGE PROFIT UP TO THE FIRST $100 PER DAY IN EXCESS OF 10 PER CENT OF CHARTERER'S CAPITAL NECESSARILY EMPLOYED IN THE BUSINESS, AND (b) 75 PERCENT OF THE NEXT $200 PER DAY, AND (c) 90 PER CENT OF ALL NET VOYAGE PROFITS IN EXCESS OF $300 PER DAY.

There was no acquiescence in the unlawful action, nor was Maritime misled by the charterers in any respect. The charterers, through their industry associations, promptly protested the sliding scale upon the specific ground that section 709(a) precluded the excess shares.[43] The district court recognized these

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[43] The protest of the Ship Operators Association, Inc., introduced as an exhibit by the United States in the *Smith-Johnson* case referred to *supra*, which was forwarded to Maritime on August 15, 1946, read in relevant part as follows:

> 2—RESOLVED, that it is the consensus of opinion of the members of this Association that the recapture of the profits under the proposed form of bareboat charter is not commensurate with the risks which the charterer assumes under his charter party and the Association under Title 7 Section 709 of the Merchant Marine Act of 1936 questions the legality of the Commission's right to recapture more than 50% of the net

protests,[44] and the Government conceded in *American-Foreign* that the charters were amended in recognition of the protests.[45] The rights of the charterers,

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voyage profits in excess of 10% per annum and in behalf of its members the Association, reserves all rights under such section.

The McDaniel affidavit in *Smith-Johnson, supra,* stated in part:

> By telegram of August 15, 1946, the Committee of the Whole, representing the American Merchant Marine Institute, Inc. (herein called "AMMI"), the Association of American Shipowners, the Pacific American Steamship Association, and the Shipowners Association of the Pacific Coast stated the unanimous opinion that
>
> proposed rate of additional charter hire exceeds rate authorized by applicable law. (p. 51a)

[44] R. 13 and 202 F. Supp. at 302-303:

> 6. Eastern has continuously since August 15, 1946, when it joined with other members of the American Merchant Marine Institute, Inc. in a telegram to the Commission, protested that the rates of so-called "additional charter hire" specified in Part II Clause 13 of the standard contract exceed the rate authorized by applicable law. Although Eastern executed Contract No. MCc-41881, including Part II Clause 13, and made payments pursuant thereto, it has always relied on the Commission's assurance in Supplement 8 to General Order No. 60, particularly 46 C.F.R. 299.31(k)(1), that "neither the tender" of payments "by the charterer, nor its acceptance by the Commission, shall prejudice the rights of either under the applicable bareboat charter agreement or otherwise."

[45] The Government's brief to the Court of Appeals in *American-Foreign* dated November 29, 1960, stated:

> The terms of the re-written agreement (on the protest of the charterers so as to make clear that they could sue at once) ....
>
> • • • •
>
> Because of the dispute as to possible violation of the statutes, Maritime changed the language [of the charter] to make it even clearer that suit should be filed at once.
>
> • • • •
>
> The form 303 (*as modified above because of the charterers'*

accordingly, must be judged on the basis of what the agency actually did, not what it could have done.

The court below was clearly wrong in relying upon a presumption of regularity, which is contradicted by the record, and in affirming what was done under the doctrine that an appeals court may affirm a district court for being right but for the wrong reason (R. 252). The statute here relevant imposes limitations upon the substance of agency action as well as the method under which that action is exercised. The courts may set aside agency action which conflicts directly with statute, but they may not correct retroactively defects in agency procedure which have been protested, and which affect substantive rights.

Petitioners not only contend that Maritime transcended the statutory limitation upon the substance of the action it took in modifying the fifty-fifty profit

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protests) was duly executed by each appellant here under further protests. (pp. 46, 48 and 49)

See also *American Mail Line, supra*, 213 F. Supp. at 157.

On May 14, 1951, Maritime sent a circular letter to all charterers, stating (R. 98):

> Where a voucher check is tendered by the Charterer, it is requested that no reference be made thereon through restrictive legend or otherwise to the effect that it is a final settlement. The accompanying letter of transmittal should state that the remittance is *on account* of additional charter hire due the Maritime Administration and is subject to adjustment upon the completion of final accounting between the Charterer and the Maritime Administration and that neither the tender of such payment by the Charterer, nor its acceptance by the Maritime Administration shall be construed as an approval of the correctness of the amount thereof, nor as a waiver of the rights or remedies of either party under the terms of the agreements involved or otherwise. [The phrase "on account" emphasized by Maritime.]

sharing requirements, but they also contend that even if the sliding scale could be considered to be within the scope of the authority granted by subsection (b) of section 5, Maritime's failure to make the statutory determination in the manner contemplated by that section creates a defect which cannot be cured by the court. The petitioners' rights must be judged solely in the light of the action taken by Maritime and not by a hindsight view of what Maritime might have done. As was said in *SEC* v. *Chenery Corp.*, 332 U.S. 194, 196 (1947):

> When the case was first here, we emphasized a simple but fundamental rule of administrative law. That rule is to the effect that a reviewing court, in dealing with a determination or judgment which an administrative agency alone is authorized to make, must judge the propriety of such action solely by the grounds invoked by the agency. If those grounds are inadequate or improper, the court is powerless to affirm the administrative action by substituting what it considers to be a more adequate or proper basis.

And more recently in *Bell* v. *United States*, 366 U.S. 393, 412-13 (1961), this Court said:

> The simple fact is that no such administrative determination has ever been made. . . . The Army cannot rely upon something that never happened, upon an administrative determination that was never made, even if it be assumed that such a determination would have been permissible under the statute and supported by the facts. . . .

In *Vitarelli* v. *Seaton*, 359 U.S. 535, 546-47 (1959), in the separate opinion by Justice Frankfurter it was pointed out:

> An executive agency must be rigorously held to the standards by which it professes its action to

> be judged. See Securities & Exch. Com. v. Chenery Corp. 318 US 80, 87, 88, 87 L ed 626, 632, 633, 63 S Ct 454. Accordingly, if dismissal from employment is based on a defined procedure, even though generous beyond the requirements that bind such agency, that procedure must be scrupulously observed. See Service v. Dulles, 354 US 363, 1 L ed 2d 1403, 77 S Ct 1152. This judicially evolved rule of administrative law is now firmly established and, if I may add, rightly so. He that takes the procedural sword shall perish with that sword.

And most recently in *Burlington Truck Lines* v. *United States,* 371 U.S. 156 (1962), this Court held that it "may not accept appellate counsel's post hoc rationalizations for agency action." See also *NLRB* v. *Atlanta Metallic Casket Co.,* 205 F. 2d 931, 936 (5th Cir. 1953):

> With regard to the suggestion that the Board in its discretion might have insured the validity of the present proceedings and order by filing either a new or later complaint, we deem it appropriate to observe that the jurisdictional issue can properly be resolved only in the light of the action taken, and not by a hindsight view of what the Board might have been authorized to do had its discretion been lawfully exercised. The Board, like all statutory and administrative agencies, is governed strictly by the statute from which it derives its existence, and equitable considerations in support of its jurisdiction are inappropriate for judicial inquiry where such jurisdiction was not properly invoked or does not otherwise exist.

Thus, judging the propriety of Maritime's action upon the grounds invoked by it to support the sliding scale charge, that charge cannot be sustained.

E. If the Excess Profit Percentages Are Authorized by Section 5(b), They Must be Deducted before Computing the 50 Percent Due under Section 709(a)

To show that the charterers' position does not (as the court below suggested) involve a matter of form rather than substance, petitioners refer to the different method of accounting for additional charter hire which must be followed if the sliding scale charge were adopted under subsection (b) of section 5, or if it were determined that the charge might be retroactively validated under subsection (b) although in fact made under section 709(a).

Section 709(a) provides that the equal division of profits is to be made "*after payment of the charter hire reserved in the charter . . .*". The "charter hire reserved in the charter" is the type of charter hire fixed under section 5(b). If the 25 and 40 percent portions of profits in excess of 50 percent had been fixed, or may now be justified, under section 5(b) then these portions (just as the 15 percent basic hire) must be deducted before dividing the remaining profits equally under section 709(a). A computation on this basis results in petitioners' additional charter hire being reduced by one-half of the 25 and 40 percent portions of additional hire claimed by the Government.[46]

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[46] The computations are contained in the supplemental affidavit of Robert Caswell (R. 40-43). This reduction in hire would be sufficient to eliminate entirely the claim of $64,000 asserted in the Government's cross-libel.

This result can most easily be illustrated by pointing out that for each dollar of additional hire in the 90 percent bracket, the 40 percent charged under section 5(b), or 40¢, would first be paid to Maritime as "charter hire reserved in the charter," and then the remaining 60¢ would be divided fifty-fifty, giving Maritime a further 30¢. This would result in profit sharing hire of 70¢ out of each dollar, instead of the 90¢ extracted under Maritime's form of charter, which disregards the statutory plan of sections 5(b) and 709(a).

Unless this is done, there is a further clear departure from the statutory plan set by section 5.

The Government in earlier cases admitted[47] that this accounting adjustment was required under the statutory formula set by sections 5(b) and 709(a). It even computed the exact amounts of the 25 and 40 percent hire which should be deducted in the present case as "charter hire reserved."[48] When it was pointed out,

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[47] In the Court of Claims, in its reply brief filed January 23, 1961, in *New York & Cuba Mail Steamship Company* v. *United States*, 290 F. 2d 925 (1961), the Government stated:

> Plaintiff next criticizes the Government's position by asserting (reply memorandum, p. 10) that the 25 and 40 percent portions of additional charter hire should have been deducted before computing the statutory 50 percent portions. *The Government agrees with this contention* but points out that it goes only to the proper method of accounting for charter hire and not to the merits of the Government's claim. (p. 15)

[48] The Government's brief filed November 22, 1960, in the district court stated, without equivocation:

> Eastern Gas regularly paid the Clause C.(1) "fixed" or "basic" hire stipulated in the charters. And on March 31, 1947, Eastern Gas submitted a typical preliminary accounting for "additional charter hire" (Exhibit L 2) due under Clause 13. That tentative accounting indicated that $10,020.00 was then due the Commission as total profit sharing and clearly showed *said sum to be composed of $5,010.00 due as 50% statutory additional charter hire under section 709(a), a further $1,550.00 due as 25% contractual additional charter hire, and a further $1,683.00 due as 40% "percentage lease" or contractual additional charter hire* under the sliding scale excessive profit sharing provision of Clause 13 (Exhibit L 2). (pp. 17-18)
>
> • • •
>
> As shown by the affidavits of Charlie H. McDaniel and former Commissioners Raymond S. McKeough, John M. Carmody and William Ward Smith, 50 percent "additional charter hire" provided for in [a] above was the required minimum *statutory* additional charter hire of section 709(a). *And, as that*

however, that this would affect the amount of additional charter hire, it submitted a lengthy affidavit which had been filed in another case (R. 122-135), stating that the excess portions of additional charter hire, originally alleged to be 25 and 40 percent, should be recomputed, upon the basis of complex mathematical formulae at 50 and 80 percent of the amount in excess of 50 percent, so as to produce the same result as that reached by taking a flat 50-75-90 percent of profits without prior deduction of any part thereof.

The Court of Claims in *American Export* (291 F. 2d at 931) and Judge Dimock in *Dichmann* (144 F. Supp. at 926) recognized that any charge made under section 5(b) would have to be first deducted before computing additional charter hire due under section 709(a), and that Maritime's failure so to provide clearly showed that no part of the sliding scale was in fact charged under section 5(b).

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affidavit explains, the further "additional charter hire" provided for in [b] and [c] above was a combination of the same 50 percent minimum required under 709(a) with added contractual elements of 25 and 40 percent prescribed under section 5(b). Thus, the added 25 and 40 percent portions (of the 75 and 90 percent items) of the [b] and [c] "sliding scale" of additional charter hire, together with the "basic charter hire," constituted the total contractual "charter hire" authorized to be charged by section 5(b). (Emphasis on *statutory* supplied by the Government)

It results that the combined firm or "basic hire" and the 25 and 40 percent portions of [b] and [c] constituted the total "charter hire reserve in the charter" as referred to in section 709(a). Never has the Government contended that the 25 and 40 percent portions of the 75 percent and 90 percent sliding scale which Eastern Gas attacks was charged under section 709(a) or otherwise than under section 5(b). (pp. 57-58)

The district court below avoided the Government's affidavits by holding that the statutory phrase "charter hire reserved in the charter" was intended to refer only to a fixed, but not to a contingent charge, such as a share of profits, made under section 5(b). It suggested that the language "charter hire reserved" should not be read literally insofar as the sliding scale was concerned, because the incorporation of section 709(a) into the 1946 Act was a "typical patch-work job." (R. 20; 202 F. Supp. at 306)

The court of appeals below misunderstood the charterers' argument with respect to the "charter hire reserved" language of section 709(a). It said that the logical conclusion of the argument was that not only the 25 and 40 percent portions in excess of 50 percent, but also the 50 percent profit payment, would have to be deducted as "charter hire reserved in the charter" before division of the remaining profits (312 F. 2d at 211). This conclusion does not follow however. Only that part of the profits in excess of the 50 percent which have their statutory basis in section 5(b) are to be deducted. The 50 percent portion admittedly has its statutory basis in section 709(a).

It is submitted that the reason why the language "charter hire reserved in the charter" in section 709(a) does not refer to a profit sharing arrangement, is that the only profit sharing arrangement contemplated by both the 1936 and 1946 Acts was that contained within the confines of section 709(a).

II. THE ADDENDUM TO THE CHARTER DIVIDING THE YEAR 1947 INTO TWO PARTS AS OF SEPTEMBER 1 VIOLATED THE CALENDAR YEAR ACCOUNTING REQUIREMENTS OF SECTION 709(a) AND WAS THEREFORE INEFFECTIVE

A. The Facts Demonstrate That the Addendum Was Not a Separate Charter But Was Imposed for the Sole Purpose of Changing the Calendar Year Accounting Plan Specified in Section 709(a)

As hereinabove recited, in mid-1947 a decline occurred in shipping and Maritime became concerned lest its excessive shares of profits accrued during the early part of that year be diluted by losses anticipated later in the same year. Accordingly, on August 15, 1947, it notified the charterers (R. 27) that their continued use of government vessels would be terminated in accordance with the fifteen days' notice provision contained in the charters, but that they would be given an opportunity to continue the use of the vessels under conditions to be announced. On August 20, 1947, Maritime informed the charterers that the vessels might be continued under charter, providing the charterers would agree within seven days to sign an addendum by which the calendar year 1947 would be divided into two parts for accounting purposes, as of September 1 (R. 28). Such an addendum (called the "Foreign Trade Addendum") was executed by petitioners, effective September 1, 1947, embodying the foregoing (R. 198-200).

The Government contends that Maritime had an absolute right to terminate the original charters under clause 14 (R. 184), that the addendum was in fact a separate charter, and that the divided accounting was properly imposed by threatened exercise of that right.[49]

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[49] The Foreign Trade Addendum was upheld as a separate charter in *American President Lines, Ltd. v. United States*, Appendix A, pp. A11-A12.

The district court below treated the Government as being in the same relation to the charterers as landlord to tenant, analogizing that a landlord might exercise his power to terminate a lease even if the purpose was to obtain a higher rental from the same tenant (R. 33). The court of appeals below did not follow this reasoning, but held the divided accounting lawful, on the same ground which it adopted in upholding the sliding scale. This was that section 709(a) should be construed to set minimum terms for the benefit of the Government, and that Maritime was empowered under subsection (b) of section 5 of the 1946 Act to change the calendar year accounting provisions to the detriment of the charterers (R. 259-60).

There is no dispute about the objective of Maritime in seeking the divided accounting. It is described in its annual report to Congress for the fiscal year ended June 30, 1948, as follows:

> On August 15, 1947, notice of termination was served on all bareboat charterers of Maritime Commission vessels effective September 1, 1947, subject to continuance under the following terms and conditions:
>
> 1. The rate of basic or additional charter hire remained unchanged.
>
> 2. The time limit of the charter was to be extended for a period of about 6 months, but no voyages were to commence after February 29, 1948, subject to termination on 15 days' notice by either party after 60 days from September 1, 1947, or from the date the vessel was delivered to [by] the Commission thereafter.
>
> 3. Payment of additional charter hire was to be computed separately for those voyages which began prior to September 1, 1947, and for those

which began under the amended terms of the charter agreement.

This action was designed to require the charterer to carry on all operations after August 31, 1947, without offsetting future losses against additional charter hire due the Government, from voyage profits for the prior period. . . (pp. 13-14)

That the Foreign Trade Addendum was not a "separate charter" is clearly apparent from the fact that it was an "addendum" to an existing charter, and was only to be "treated for accounting purposes *as if* it constituted a separate charter" (R. 198-200). Further, as its preamble notes, although a termination notice was served under the original charter, the charterers were "simultaneously advised" that they would be given an opportunity to continue the use of the vessels.

None of the events which are characteristic of a new charter took place. The vessels were not redelivered and their use was uninterrupted. No redelivery surveys were made, no redelivery repairs performed, and no inventory taken, as contemplated by the original charter. (See standard clauses at 46 C.F.R. § 299.130) Furthermore, in accounting for additional charter hire, the reserves which the charterers carried on their books for potential repair expenses and insurance losses which they expected to incur at the time of redelivery, together with other expenses which could not be allocated to a specific voyage or accounting period, were spread over the entire term of the charters both before and after September 1, 1947. (46 C.F.R. § 299.35, 299.50(b), 299.51 and 299.52(c))

As further evidence that Maritime was not seeking a bona fide termination of the charters, the Foreign

Trade Addendum provided that the charterers might not thereafter exercise the right of termination under clause 14 of the original charters before the expiration of sixty days from the effective date of the addendum on September 1, 1947 (R. 198-99). Thus, if pre-September 1 subcharter commitments were completed early in this sixty-day period, the vessels would have to be maintained in idle status at considerable expense to the charterers (including payment of "basic charter hire") until that period expired.

In summary, all of the terms of the original charter continued as before except for the divided accounting in 1947. The Foreign Trade Addendum was not "a separate charter," but a continuation of an existing charter. Its sole purpose was to create two accounting periods during the calendar year 1947 for computing additional charter hire.

B. Section 709(a) Prescribed a Mandatory Calendar Year Accounting Period

Section 709(a) provides for the computation of additional charter hire.

> . . . *whenever, at the end of any calendar year subsequent to the execution of such charter,* the cumulative net voyage profits . . . shall exceed 10 per centum per annum on the charterer's capital necessarily employed in the business of such chartered vessels, . . .

This language plainly requires a computation based upon the period commencing with "the execution of such charter" and terminating with "the end of any calendar year" subsequent thereto. Hence, when operations under a charter commence during and extend beyond the end of any given calendar year, the

first computation is made at the end of that year. Similarly, when operations extend over a period of years, a computation is made at the end of each calendar year.[50]

The legislative history makes it clear that one of the purposes of Congress in adopting section 709(a) and related sections of the 1936 and 1946 Acts was to modify insofar as possible the impact of the abnormal cyclical fluctuations which were characteristic of the shipping business. It intended that periods of profits and losses should be averaged for purposes of computing "additional charter hire" under section 709(a) as well as for purposes of recapture of profits by the Government under operating-differential subsidy agreements. Thus, at the hearings which preceded enactment of the 1936 Act, a spokesman for the industry said:[51]

> The shipowner has got to have a possible hope of accumulating earnings and reserves in the good

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[50] The term "net profits" used without qualifying language normally implies a calendar year computation. *Laystrom* v. *Continental Copper and Steel Industries*, 133 F. Supp. 130, 133 (N.D. Ill. 1955), *aff'd*, 244 F. 2d 504 (7th Cir. 1957). Here, section 709(a) expressly fixes the calendar year basis and nothing is left to implication. The Government concedes that the term "net profits" in section 709(a) requires a combining of the results of profits and losses from all voyages terminated within each calendar year. See petition for certiorari of the Solicitor General in *United States* v. *Moore-McCormack Lines, Inc.*, No. 862—October Term, 1962 (pp. 10-11). The purpose of the word "cumulative" in section 709(a) was to require the offset of profits in one calendar year against losses in other years over the term of any charter to which that section applies. *United States* v. *Moore-McCormack Lines, Inc.*, 308 F. 2d 866, 871 (4th Cir. 1962), *cert. denied*, 372 U.S. 944 (1963).

[51] Hearings before the Senate Committee on Commerce on S. 2582, 74th Cong., 1st Sess. p. 167 (1935).

periods to make up the losses in bad periods. It is a business of peaks and hollows.

This observation was confirmed by Senators White and Fletcher in the same hearings, as follows (*id.* at 318-19):

Senator White. Otherwise, in the fat years, you could not make provisions for the lean years.

Mr. Smith. In fat years you are turning money back, and in lean years you are taking a loss.

Senator White. If you cannot make provision in the fat years for the lean years, which are inevitable, you cannot get ahead.

Mr. Smith. That is true.

Senator Fletcher. In other words, you want to make it attractive to private capital to invest in shipping?

Mr. Smith. Yes.

Section 606(5) of the 1936 Act originally provided for offset of profits and losses over a five-year period in computing recapture under subsidy agreements but Congress in 1938[52] increased this period to ten years.

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[52] Section 606(5) of the 1936 Act, as amended by Act of June 23, 1938, c. 600 § 22, 52 Stat. 960 (46 U.S.C. § 1176), provides:

> that when at the end of any ten-year period during which an operating-differential subsidy has been paid under a contract or consecutive contracts . . . if the net profit of the contractor on his subsidized vessels and services incident thereto during such period or time . . . has averaged more than 10 per centum per annum upon the contractor's capital investment necessarily employed in the operation of the subsidized vessels, services, routes, and lines, the contractor shall pay to the United States an amount equal to one-half of such profits in excess of 10 per centum per annum as partial or complete reimbursement for operating-differential subsidy payments . . .

The Senate committee report explaining this amendment stated (S. Rep. No. 1618, 75th Cong., 3d Sess. p. 15 (1938)):

> A study of the financial history of the steamship business indicates that such incidents are characteristic of the industry. Profits, while large in some instances and in others enormous, during prosperous periods, are usually counterbalanced by equally large or enormous losses in depression years. The proposed amendment recognizes this fact, and adapts the recapture provisions to the cyclical nature of the industry.

Since section 709(a) was modeled after the subsidy recapture provisions, it is fair to attribute the same purpose to both[53] and Maritime's action in requiring separate accountings for profitable and unprofitable periods clearly frustrates this purpose. If Maritime has the power to modify the calendar year accounting provisions of section 709(a) or the subsidy recapture provisions in the 1936 and 1946 Acts, it will undermine this clearly expressed congressional policy.

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[53] The provision for calendar year accounting originated in section 530 of S. 3500, 74th Cong., 2d Sess. (1936). (Committee Print of March 3, 1936) (the Copeland bill). Similar language was also contained in section 35 of S. 4110, 74th Cong., 2d Sess. (1936) (the Guffey bill print of February 24, 1936). That print of the Guffey bill contained a chartering provision (Appendix B, pp. B1-B2) which specified no accounting period for the determination of profits from charters, and also contained subsidy recapture provisions paralleling those of the Copeland bill, including calendar year accounting. The print of the Guffey bill containing section 709(a) in the form in which it was finally enacted (section 47 of S. 4110, Committee Print of March 30, 1936) contained parallel provisions for subsidy recapture and additional charter hire, both calling for calendar year accounting. See *United States* v. *Moore-McCormack Lines, Inc.*, *supra*, 308 F. 2d at 872, ftn. 13.

In *United States* v. *Moore-McCormack Lines, Inc., supra,* Maritime sought by regulation to eliminate the year-to-year cumulation of profits and losses under a charter similar to that of petitioners, and the court pointed out that Congress intended that calendar year profits and losses should be offset against each other over the entire period of the charter, irrespective of the sequence in which they occurred, because of the cyclical nature of the shipping business (308 F. 2d at 873).

The court below relied upon subsection (b) of section 5 as justifying the change in the calendar year requirement of section 709(a). But the language of the former section can hardly be interpreted to empower the Commission to fix an accounting period, or to modify the period set by section 709(a). Section 5(b) says that "charter hire . . . shall be fixed by the Commission *at such rate* as the Commission determines to be consistent with the policies of this Act, but . . ." etc. The establishment or changing of a statutory accounting period does not have any logical relation to the fixing of a "rate" of the type authorized or contemplated by section 5(b).

Nor may the power to change the accounting period be inferred from the policy to encourage sales over charters which was relied upon by the court below in sustaining the sliding scale. Since the Foreign Trade Addendum was imposed in the face of a declining freight market, it could not induce this result.

C. The Foreign Trade Addendum Was Ineffective to Overcome the Statutory Requirement of Calendar Year Accounting

The circumstances recited above show that there was in fact no real termination of the charter and that Maritime gave notice of termination only for the purpose of circumventing the statutory requirement for calendar year accounting. The addendum was contrary to the express provisions as well as to the underlying policies of the 1936 and 1946 Acts and served no business or regulatory purpose. For purposes of section 709(a), the charter must be treated as one contract. The case is analogous to the cases where transactions having a tax avoidance motive and no legitimate business purpose have been treated as ineffective. *Gregory* v. *Helvering*, 293 U.S. 465 (1935); *Harrison* v. *Schaffner*, 312 U.S. 579, 582 (1941); *Commissioner* v. *Court Holding Co.*, 324 U.S. 331, 334 (1945). It has also been held that a clear contract right, as the right here to terminate the charters, may not be used as part of a scheme to accomplish a forbidden result. *Fidelity & D. Co.* v. *Tafoya*, 270 U.S. 426, 434 (1926). See the Ship Sales Act cases cited *supra* at p. 25, and *Clapp* v. *United States*, 117 F. Supp. 576 (Ct. Cl. 1954), *cert. denied*, 348 U.S. 834 (1954); *Suwannee Steamship Co.* v. *United States*, 279 F. 2d 874 (Ct. Cl. 1960); *Seatrade Corp.* v. *United States*, 285 F. 2d 448 (Ct. Cl. 1961). Thus, steamship companies have the power (with Maritime's approval) to enter into rate fixing agreements, but they may not exercise the power for the purpose of violating the statutory prohibition against driving an independent competitor out of the trade. *FMB* v. *Isbandtsen Co.*, 356 U.S. 481 (1958). Similarly, a seller has the power to sell his product to whomever he chooses at whatever price, but he may

not exercise the power for the purpose of effecting a violation of the anitrust laws. *United States* v. *McKesson & Robbins, Inc.*, 351 U.S. 305 (1956); *Lorain Journal Co.* v. *United States*, 342 U.S. 143, 155 (1951). As was said in *United States* v. *San Francisco*, 310 U. S. 16, 28 (1940):

> Terminology of consignment . . . , rather than . . . sale, and verbal description of the power company as the City's agent or consignee, are not sufficient to take the actions of the parties under the contract out of § 6. . . . The City has in fact followed a course of conduct which Congress, by § 6, has forbidden. Mere words and ingenuity of contractual expression, whatever their effect between the parties, cannot by description make permissible a course of conduct forbidden by law.

The district court's analogy to a landlord's termination of a tenancy for the purpose of raising the rent is not appropriate. A closer analogy would be a purported termination and renewal of a tenancy for the sole purpose and with the sole effect of evading a rent control law.

It is furthermore obvious that there was coercion exercised over the petitioners in the execution of the Foreign Trade Addendum because of pre-existing subcharter commitments for the vessels (R. 237). Some of these subcharters had been specifically approved by Maritime prior to the notice of termination on August 15, 1947 (R. 30-31). These subcharters would have been excused only if Maritime had terminated the bareboat charter in a manner which would "frustrate the performance" of the subcharters (see clause 29, R. 32). There was, however, no true termination of the bareboat charter since petitioners were per-

mitted to continue the use of the vessels, but on less favorable terms. These voyages were scheduled for imminent loading, the freight rates were favorable to the subcharterers, and the latter would certainly not relieve petitioners from liability for damages for breach of the subcharters simply because the bareboat charter terms had become more onerous. *Columbus Ry P. & L. Co.* v. *Columbus*, 249 U.S. 399, 419 (1919); *Texas Co.* v. *Hogarth Shipping Co.*, 256 U.S. 619, 630 (1921); *Gulf, Mobile & Ohio R. Co.* v. *Illinois Central R. Co.*, 128 F. Supp. 311, 323-24 (N.D. Ala. 1954), *aff'd*, 225 F. 2d 816 (5th Cir. 1955), *cert. denied*, 350 U.S. 932 (1956).

However, irrespective of coercion, petitioners may properly contest the effectiveness of the addendum because the regulations in existence at the time, hereinabove cited in ftn. 10, said that the statutes were controlling and the rights of the parties were reserved "under the applicable bareboat charter agreement or otherwise."

For the foregoing reasons, the Foreign Trade Addendum should be disregarded and the year 1947 accounted for as a single calendar year in accordance with the requirements of section 709(a).

III. CONCLUSION

Petitioners respectfully request this Court to find and determine:

(a) That petitioners were not obligated to pay "additional charter hire" in excess of 50 percent of their net voyage profits derived from operation of the chartered vessels after a 10 percent return on capital;

(b) Alternatively, that if the 25 and 40 percent portions of additional charter hire are lawful, said

excess portions of additional charter hire must be deducted as "charter hire reserved in the charter" within the meaning of section 709(a), before computing the fifty-fifty division of remaining profits due the Government;

(c) That the Foreign Trade Addendum requirement for split accounting in 1947 was contrary to the calendar year provisions of section 709(a) and is therefore invalid. Accordingly, the profits and losses sustained from all voyages completed during the calendar year 1947 may be offset against each other in determining the obligation for additional charter hire; and

(d) That the judgment of the court below in favor of the Government for $64,000 should be reversed and the case remanded, with instructions to enter judgment in favor of petitioners for the amount of additional charter hire unlawfully exacted by Maritime.

Respectfully submitted,

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